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Supreme Court of the United States

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October Term, 1974

No. 74-1230

LOUIS R. SNELLING, III,

Petitioner,

vs.

CHELTENHAM NATIONAL BANK,

Respondent.

RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI TO THE SUPERIOR COURT OF THE COMMONWEALTH OF PENNSYLVANIA

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COUNTER-STATEMENT OF THE CASE

On February 27, 1970, petitioner, Louis R. Snelling, III, (hereinafter sometimes referred to as "Snelling") executed a promissory note to Goodway Copy Centers, Inc. (hereinafter sometimes referred to as "Goodway") in the amount of $150,000, said note being the subject of this action.

Petitioner executed this promissory note for the sole purpose of securing a loan in the amount of $150,000 from Cheltenham National Bank (hereinafter sometimes referred to as "Bank"), in order to assist petitioner in financing the opening and operation of certain new copy centers in connection with a franchising agreement which had been entered into previously by petitioner and Goodway Copy Centers, Inc.

The aforesaid franchising agreement called for a substantial investment of funds on the part of Snelling, and, apparently, petitioner did not wish to risk any of his own funds in this venture due to the highly speculative nature of same. Therefore, petitioner made arrangements through Goodway Copy Centers, Inc. to use the money of Cheltenham National Bank instead.

In furtherance of this plan, on March 24, 1970, Goodway Copy Centers, Inc. assigned the aforesaid promissory note of petitioner to Cheltenham National Bank. In consideration for same, the Bank loaned to Snelling and Goodway Copy Centers, Inc. the sum of $150,000 on March 25, 1970.

At the time this loan was made to Snelling, he was a mature businessman and was serving as Senior Vice President and a Director of Snelling and Snelling, Inc., a large national employment service company, and he was the beneficial owner of more than ten percent of this company's stock. His salary was well in excess of $10,000 per year, and in addition thereto, he received certain expense account allowances, insurance, profit-sharing and stock option benefits. Further, he always had access to legal counsel and was, in fact, represented by legal counsel at that time.

The funds which were loaned by the Bank to Snelling were deposited in accounts held in the name of International Development Corporation and Goodway Copy Centers, Inc. International Development Corporation was a Pennsylvania corporation in which Snelling owned all of the outstanding shares and acted as President and Chairman of the Board and which was set up solely for the purpose of carrying on the aforesaid franchise business. Within three to four weeks thereafter, all of the aforesaid funds had been withdrawn from these accounts.

During the course of the following year, petitioner made regular monthly payments of interest on the subject loan to the Bank. No payments were made on the principal amount of the loan.

Near the end of March 1971, the Bank made demand upon Snelling and Goodway Copy Centers, Inc. to pay the principal amount of the loan together with any interest which had accrued to that time. Despite the Bank's demand, petitioner made no payments from that time to the present.

The Bank continued its efforts throughout the course of 1971 to secure payment on the principal and interest due on the loan, but all efforts failed.

In the early part of December 1971, the President of Cheltenham National Bank personally met with Snelling and Donald L. Wolk, President of Goodway Copy Centers, Inc., in an effort to resolve this matter. At this meeting, Snelling agreed to repay the principal and interest due on the loan on a payout

schedule of $20,000 initially and $25,000 quarterly thereafter until the full amount had been paid. In reliance on Snelling's representations, the Bank withheld any legal action to enforce collection of the amount due and owing to it.

A number of months passed by during which no payments were forthcoming. The Bank continued to press Snelling and Goodway Copy Centers, Inc. for payment but to no avail.

During this same period of time, the Bank requested from Snelling certain collateral to secure this debt. Snelling turned over to the Bank 18,444 shares of Snelling and Snelling, Inc. common stock which was owned by him, personally, in response to this request. Snelling claimed that the market value of this common stock at the time amounted to $75,000. An authority to pledge securities was signed by Snelling and delivered with the aforesaid stock to the Bank.

Although Snelling continuously acknowledged his debt to the Bank and continued to make numerous promises to repay same, no payments were made. Therefore, having exhausted all avenues of collection, the Bank was forced to confess judgment on the promissory note executed by Snelling.

The evidence clearly indicates that Snelling acknowledged his debt to the Bank both by his words and his actions. Snelling and/or his company, International Development Corporation, made regular interest payments on the loan during the course of the first year following the grant of the loan. Snelling agreed to make every effort to repay the debt more than one year after the loan had been granted. Further, he agreed to a pay-out schedule

after meeting with the President of Cheltenham NationalBank in the early part of 1971, more than one and one-half years after the loan had been granted. Still further, Snelling delivered to Cheltenham National Bank as collateral to secure this loan 18,444 shares of common stock of Snelling and Snelling, Inc. owned by him and having a value of $75,000, according to Snelling at that time. This stock was delivered to the Bank by Snelling two years after the loan had been granted.

Snelling never denied that this money was owed to the Bank. More importantly, he never raised any objections to repaying the money owed to the Bank nor did he ever mention any problem or defenses which existed between him and the original promisee, Goodway Copy Centers, Inc., until after the Bank had confessed judgment on the note almost three years after the loan had been made.

On April 6, 1973, after all collection efforts had failed, the Bank confessed judgment in the amount of $187,062.02 against Snelling on the warrant contained in the promissory note.

On May 16, 1973, Snelling filed his petition to open judgment which was the subject matter of proceedings in the state courts. The Bank filed a timely answer to same. Depositions of Snelling, Donald L. Wolk, President of Goodway Copy Centers, Inc., and Monroe W. Long, President of Cheltenham Bank, were taken. At these depositions, counsel for Snelling had full and complete opportunity to examine and cross-examine all the principals involved in the loan transaction. In addition, Snelling had the right to call for depositions of any other witnesses that he desired to substantiate his position and

he had the right to subpoena and make a part of the record any and all documents that he desired. He elected not to do so.

The depositions taken were transcribed and all documents entered as exhibits were copied and these were made part of the record in the case.

The case was submitted on this record and briefs and argued before the court en banc of the Court of Common Pleas of Montgomery County, Pennsylvania, on December 31, 1973; and on March 27, 1974, the court issued an order dismissing Snelling's petition to open judgment.

From this order, Snelling filed an appeal to the Superior Court of Pennsylvania, which affirmed the action of the trial court on September 23, 1974. Petitioner then applied for a writ of certiorari to the Supreme Court of Pennsylvania, which was denied on January 2, 1975.

ARGUMENT

At the outset, it is important to note that the decision of the trial court and the Superior Court of Pennsylvania, wherein Snelling's petition to open judgment was denied, was based upon an equitable estoppel and petitioner's efforts to challenge the constitutionality of the confession of judgment procedure in the Commonwealth of Pennsylvania had no bearing on the outcome of the case. (See opinion and order of the Court of Common Pleas and Superior Court of Pennsylvania, Appendix A and B of petitioner's brief.)

In his petition to open judgment, Snelling took the position that the note in question was not negotiable and that Cheltenham Bank was not a holder in due course; and as such, Snelling should be permitted to raise any defenses that he had against Goodway Copy Centers, Inc. on the original agreements and amendments between Snelling and Goodway.

The lower court decided that the note was negotiable and that the Bank was a holder in due course and that any defenses existing between Snelling and Goodway would be cut off since they were unknown to the Bank at the time the Bank took the note.

Further, the lower court, in its opinion, stated that even if the Bank was not a holder in due course of the note, by reason of Snelling's conduct and actions, he has estopped himself from asserting any defenses he may have as to Goodway against Cheltenham Bank.

The Superior Court of Pennsylvania affirmed the lower court's decision and, in its opinion, stated that Snelling was estopped from asserting defenses against the Bank, as assignee, on the basis that the facts in the case warranted an equitable estoppel.

The essential elements of an equitable estoppel as related to the party claiming the estoppel are: (1) lack of knowledge and of the means of knowledge of the truth as to the facts in question; (2) reliance upon the conduct of the party estopped; and (3) action based thereon of such a character as to change his position prejudicially. *United States National Bank in Johnstown v. Drabish,* 187 Pa. Superior Ct. 169.

Cheltenham Bank waited more than three years from the time it obtained the note until it confessed judgment. This forebearance on the part of the Bank was caused directly by the promises and actions of Snelling indicating clearly that he acknowledged the debt and would pay same.

This delay resulted in a prejudicial change in Cheltenham Bank's position, as outlined in the opinion of the Superior Court of Pennsylvania, and as indicated hereinafter.

Further, the aforesaid opinions and orders of the Court of Common Pleas of Montgomery County and the Superior Court of Pennsylvania were left standing by the Supreme Court of Pennsylvania when it denied petitioner's petition for an allowance of appeal to that Court.

In his brief, petitioner argues erroneously that, in the Commonwealth of Pennsylvania, the procedure for opening judgment may impose an undue burden of proof upon the defendant. This is not the case at all.

In fact, Rule 2959 of the Pennsylvania Rules of Civil Procedure was amended October 4, 1973, effective December 1, 1973, changing the burden of proof in Pennsylvania and adopting the Ohio procedure which requires opening where evidence is presented which, in a jury trial, would require the issues to be submitted to the jury. (See Appendix A herein.)

Under the Pennsylvania Rules of Civil Procedure, Rule 236, the Prothonotary of the Court shall immediately give written notice to the defendant when a judgment is entered by confession. (See Appendix B herein.)

Relief from a judgment by confession may be sought by filing a petition to open or strike the judgment. The court may stay all proceedings meanwhile.

The defendant then has full opportunity to take the testimony of all witnesses that he may desire, either by hearing or by depositions, and he may secure the production of all admissions, documents, and other evidence that he may desire to support his position. Subpoenas may be issued to enforce the appearance of witnesses or to secure the production of documents. Briefs are submitted and the case is then argued before the court en banc. If evidence is produced which in a jury trial would require the issues to be submitted to the jury, the court then must open the judgment. (See Rule 2959, Appendix A herein.)

Further, it should be noted that in Pennsylvania under the Act of January 30, 1974, Act No. 6 of 1974, P.L. , no execution may be had on any confessed judgment secured as a result of any document containing a confession of judgment clause, which, when confessed, effects a lien upon real estate, until the plaintiff therein have commenced an action and proceeded to judgment against defendant as in any original action, which judgment is then merged with the confessed judgment and execution may then, and only then, be issued on the confessed judgment.

Rule 2959 was amended to provide a major change in Pennsylvania practice. This rule was in effect at the time when this case was argued before the court en banc of the Court of Common Pleas of Montgomery County, Pennsylvania, on

December 31, 1973, and prior to the court's issuing its opinion and order dismissing petitioner's petition to open judgment on March 27, 1974.

Historically, it has been the rule in Pennsylvania that the opening of a confessed judgment is a matter within the discretion of the Common Pleas Court and the Appellate Courts will not reverse unless there has been an abuse of discretion. It placed upon the defendant the burden of persuading the court to open the judgment.

The amendment to Pennsylvania Rule of Civil Procedure 2959(e) meets the criticism of the United States Supreme Court in the cases of *D.H. Overmyer Co. v. Frick Co.*, 405 U.S. 174 (1972) and *Swarb v. Lennox, et al.*, 405 U.S. 191 (1972), stating specifically that, if the defendant produces evidence, which, in a jury trial, would require the issues to be submitted to a jury, the court shall open the judgment.

There were certain other amendments to the confession of judgment rule on October 4, 1973, which were clarifying or technical in nature, but have no bearing on the issue in this case. This is brought to the attention of the court due to the fact that the Rules of Civil Procedure contained in Appendix C of petitioner's brief are inaccurate and do not contain the various amendments to these Rules as indicated herein.

Since this court has not held that confession of judgment without notice and opportunity for hearing pursuant to warrants of attorney are void, nor has it held that statutes and rules authorizing confession pursuant to warrants of attorney are void

per se or facially unconstitutional or is violative of due process requirements of prior notice and opportunity for hearing, petitioner's challenge in this particular case is totally unwarranted.

On the contrary, in *Overmyer, supra,* this court held that due process rights in civil matters could be knowingly, intelligently and voluntarily waived. It has suggested that "contracts of adhesion" in which there is an inequality of bargaining power and lack of consideration for the waiver are factors to be considered in determining whether contractual waivers in consumer transactions were voluntarily, knowingly and intelligently entered into.

Where, in *Overmyer,* as in this case, a warrant for confession of judgment was part of a commercial transaction between parties of equal bargaining ability and supported by consideration, it is clear that there was a valid contractual waiver of due process rights voluntarily, knowingly and intelligently made.

Here, the loan made to petitioner was part of a commercial transaction supported by consideration specifically bargained for. Petitioner was a sophisticated, experienced businessman who was serving as Senior Vice President and member of the Board of Directors of Snelling and Snelling, Inc., a large national employment service company, at the time he entered into the loan transaction; and he had ready access to legal counsel.

In *Fuentes v. Shevin,* 407 U.S. 67 (1972) and *Overmyer, supra,* which are relied upon by petitioner, it is apparent that the

contract of adhesion concept used in the consumer field does not really apply to commercial transactions between businessmen and corporations. It is apparent that the court has clearly recognized that important commercial interests require some form of pre-judgment remedy.

Although due process concepts may be proper in certain situations, they are certainly not appropriate in the field of commercial transactions. Inasmuch as the case at bar is one involving a commercial transaction and one involving a sophisticated experienced businessman, there is no reason to invalidate the confession of judgment c'ause in this case.

Further, there is some question that there is the requisite state action under the due process clause of the Fourteenth Amendment in the confession of judgment procedure in Pennsylvania, and particularly in this case. It would seem that the involvement of the state in this procedure is only passive and not significant. The procedure merely allows for a certain act of a private individual to occur; and active or direct state action which exists when the statute compels an event or a state official acts in concert or on behalf of an individual in performing the act on which the complaint is based, is not present in this procedure. Also, no property is seized or taken from the debtor as a result of the entry of judgment.

It is clear that in this case, petitioner was not rendered defenseless by execution of the cognovit note. He successfully avoided payment of his obligations for three years during which time Cheltenham Bank forbore from taking any action on the note due to petitioner's promises to pay. He has continued to

successfully avoid payment of his obligation for an additional two years since Cheltenham Bank confessed judgment on the note. All of this has been to the prejudice and damage of Cheltenham Bank inasmuch as Goodway Copy Centers, Inc. has sold all of its assets and gone out of business, International Development Corporation has no assets and is no longer in business and the Snelling and Snelling, Inc. stock pledged as collateral by petitioner has been severely depressed in value; and petitioner has gained a substantial amount of time within which to dispose of his valuable assets. The difficulty of obtaining the payment is self-evident.

CONCLUSION

For these reasons, respondent respectfully requests that petitioner's writ of certiorari be denied.

Respectfully submitted,

s/ Harry C. Barbin
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Attorney for Respondent

APPENDIX A

Pennsylvania Rules of Civil Procedure

Rule 2959. Striking Off or Opening Judgment. Pleadings. Procedures.

(a) Relief from a judgment by confession shall be sought by petition. All grounds for relief whether to strike off the judgment or to open it must be asserted in a single petition.

(b) If the petition states prima facie grounds for relief the court shall issue a rule to show cause and may grant a stay of proceedings. After being served with a copy of the petition the plaintiff shall file an answer on or before the return day of the rule. The return day of the rule shall be fixed by the court by general rule or special order.

(c) A party waives all defenses and objections which he does not include in his petition or answer.

(d) The petition and the rule to show cause shall be served as provided in Rule 233, and the answer as provided in Rule 1027.

(e) The court shall dispose of the rule on petition and answer, and on any testimony, depositions, admissions and other evidence. The court for cause shown may stay proceedings on the petition insofar as it seeks to open the judgment pending disposition of the application to strike off the judgment. If evidence is produced, which, in a jury trial, would require the issues to be submitted to the jury, the court shall open the judgment.

APPENDIX B

Pennsylvania Rules of Civil Procedure

Rule 236. Notice by Prothonotary of Entry of Order, Decree or Judgment.

(a) The prothonotary shall immediately give written notice by ordinary mail of the entry of any order, decree or judgment:

(1) When a judgment by confession is entered, to the defendant at his address stated in the certificate of residence filed by the plaintiff; and

(2) In all other cases, to each party who has appeared in the action or to his attorney of record.

(b) The prothonotary shall note in the docket the giving of the notice.

(c) Failure to give the notice shall not affect the lien of the judgment.